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When Key Employees Go to Competitors

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Litigation

As the economy recovers, employers are increasing their efforts to hire additional key employees. Many key employee hires are coming from competitors, or companies in similar fields, that are located in California or in other states. Such hiring means the companies losing employees are increasingly concerned about how to protect their trade secrets and their remaining employees. As a result, companies are increasingly crying foul, and considering litigation when a key employee is hired away. In this environment, hiring companies should be more cautious and consider taking early steps to minimize the potential litigation risks associated with key employee hires.

As such litigation increases, both former and new employers are smart to recognize that litigation over employees and trade secrets is often messy, expensive and potentially disruptive. Here are five tips to consider when facing these issues:

1. REVIEW CONTRACT PROVISIONS

Most companies now have provisions in their employment contracts limiting what an employee can do when she leaves for a new job. These provisions can include: 1) noncompetition provisions; 2) nonsolicitation provisions for employees, customers or others; 3) confidentiality provisions; and 4) trade secret provisions. Such provisions often vary in their purported time limitations or scope, ranging from relatively well-defined, short time-period limitations to broad, long time-period limitations.

As hiring increases, companies losing key employees should review their employment agreements to ensure they include as many enforceable provisions as possible. While some courts will narrow an overbroad provision in litigation, the existence of an overbroad provision almost always provides a decent argument that the restriction is void and unenforceable. Thus, for example, although California law allows some nonsolicitation provisions (if they are reasonable in time and scope, etc.), broader nonsolicitation provisions can be challenged as violating California Business and Professions Code §16600's prohibition against noncompetition agreements. *See Metro Traffic Control, Inc. v. Shadow Traffic Network*, 22 Cal.App.4th 853 (1994).

Companies hiring key employees should review any potential candidate's existing employment agreement(s) early in the interview process to assess whether she is subject to potentially valid noncompetition, nonsolicitation, confidentiality or trade secret provisions. Hiring companies should also assess whether a candidate's former work was done exclusively or primarily in California because §16600 invalidates noncompetition agreements for California employees or for those whose work is carried out substantially in California. *See, e.g., Frame v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 20 Cal.App.3d 668 (1971). If a candidate is subject to potentially valid limitations, the hiring company should decide early whether it could employ the candidate in a way that does not violate such limitations or could live with the job restrictions that may be needed to accommodate such limitations.

2. PROTECT TRADE SECRET INFORMATION

In any state, the strongest potential claims against a future employer or key employee are claims that the departing employee took trade secrets or will disclose them in the future. Some states have an "inevitable disclosure" doctrine, making it easier to bring a trade secrets claim if one can claim that a former employee's new position makes it "inevitable" that she will disclose trade secrets. Other states, like California, reject this doctrine but still allow such claims if a former employer can prove an actual risk of trade secret misappropriation, such as by "submit[ting] evidence beyond [a] former employee's knowledge of trade secrets and subsequent change of employers." *Les Concierges, Inc. v. Robeson*, 2009 WL 1138561 (N.D. Cal. 2009) (applying California law).

For companies losing key employees, it is important to have policies that define what company information is considered to be confidential or a trade secret. It is also important to develop policies and procedures that help ensure (and can prove) that certain information is treated as a "trade secret" or confidential. As key employees depart, companies should consider implementing a process to determine whether each such employee had access to trade secret/confidential information, whether she is taking such information or likely to use it at her new job, and whether the employee or her information is important enough to spend time and money to litigate. Companies should also assess whether to gather the evidence needed to prove a trade secret claim against a departing employee and consider procedures to capture potentially relevant information on computers, emails, etc.

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Hiring companies are smart to try and prevent the transfer of confidential/trade secret information at the outset. Thus, hiring companies should review whether and how they caution interviewing candidates about discussing a former employer's information with interviewers and about the need not to disclose any confidential/trade secret information during the interview process. Additionally, hiring companies should review their procedures for training new employees to ensure that incoming employees are reminded about pre-existing confidentiality/trade secret obligations, reminded not to transfer such information and informed about the policies or procedures designed to prevent such transfers.

3. EARLY NEGOTIATIONS TO RESOLVE CONCERNS

When a key employee tells a current employer that she is moving to a competitor, this often starts a flurry of letters, or litigation threats, between the companies. However, since litigation over employees and trade secrets can be expensive and disruptive to both sides, it is important to consider, at the outset, whether companies can resolve disputes over a key employee via a negotiated agreement, rather than litigation.

When companies try to talk first, the parties may be able to negotiate an early agreement over a key employee that neither will love, but both can live with. Negotiating such agreements only works when neither side is driven by emotion or a desire to prove a point, and when both sides are willing to engage in detailed negotiations over possible compromise solutions, and can be trusted to honor their commitments. However, where such factors exist, the types of agreements reached via early negotiations often closely mimic the agreements that could be reached as a settlement after litigation has been filed, without incurring litigation costs or the business disruptions of litigation.

To negotiate such agreements, both the former and hiring employers should consider who should handle them. At times, outside counsel may be best, while at other times such negotiations are best handled by in-house counsel who have ongoing relationships with each other. However, even if negotiations are handled in house, both employers should consider engaging outside counsel who can advise on, and document, the agreements and can advise on any potential litigation issues that may be relevant. Additionally, the hiring employer should consider whether the key employee needs her own counsel in order to ensure that she is confidentially and properly advised about her ongoing obligations and any obligations under the newly negotiated agreement and to assist in the negotiation process.

4. CONSIDER JURISDICTION ISSUES

Most states other than California allow noncompetition agreements if they are reasonable in scope, and sometimes, if they are designed to protect against illegal or unfair conduct. Thus, if a hired key employee is moving from a non-California company, or worked outside of California, a former employer may try to enforce such agreements in a non-California court. Former employers seeking to enforce a noncompetition agreement should make an early determination about whether the departing key employee is someone worth litigating over, and if so, where to litigate any dispute. Hiring employers should take early steps to understand whether, and to what extent, a noncompetition agreement may be enforceable. Additionally, where litigation seems likely, a hiring employer should consider whether to initiate declaratory relief litigation in California to define a new employee's ongoing obligations, including whether it wants to initiate litigation that might not otherwise occur or risk a dual-forum legal battle.

5. PREVENT CONFLICTS AFTER AN EMPLOYEE LEAVES

Once a key employee has decided to move to a new employer, new and former employers can take steps to prevent future conflicts. Many former employers ask departing employees to sign an acknowledgment stating that they remember their ongoing confidentiality obligations and are not taking confidential/trade secret information. These acknowledgements can provide some comfort that such information is protected and be valuable in future litigation if such information is disclosed. For hiring employers, these acknowledgements provide an opportunity to discuss the key employee's ongoing obligations and ensure that no information has inadvertently been kept or moved. Hiring employers should also review any such acknowledgments to confirm that it does not place any additional restrictions on the employee.

Additionally, new employers can try to minimize the risk of future conflicts regarding a key employee by: 1) reminding the employee of any continuing obligations to a former employer; 2) stressing that she must follow any ongoing, nonsolicitation agreements for the requisite period of time; and 3) considering whether she should be allowed to recruit, or interview, potential candidates from the same former employer for a set period of time.

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